Supreme Court, U.S.
FILED
MAY 27 1997
CLERK

No. 96-1669

In The

Supreme Court of the United States

October Term, 1996

PADDOCK PUBLICATIONS, INC.,

Petitioner,

v.

CHICAGO TRIBUNE COMPANY, CHICAGO SUN-TIMES, INC., NEW YORK TIMES SYNDICATION SALES CORPORATION, LOS ANGELES TIMES/ WASHINGTON POST NEWS SERVICE, INC., TRIBUNE MEDIA SERVICES, INC., CREATORS SYNDICATE, KING FEATURES SYNDICATE, INC. TIMES MIRROR COMPANY d/b/a LOS ANGELES TIMES SYNDICATE, UNITED MEDIA, and UNIVERSAL PRESS SYNDICATE,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Seventh Circuit

REPLY TO BRIEF IN OPPOSITION

LEE A. FREEMAN, JR.
Counsel of Record
JAMES T. MALYSIAK
FREEMAN, FREEMAN & SALZMAN, P.C.
401 North Michigan Avenue,
Suite 3200
Chicago, Illinois 60611-4207
(312) 222-5100

Counsel for the Petitioner

COCKLE LAW BRIEF PRINTING CO., (800) 225-6964
OR CALL COLLECT (402) 342-2831

TABLE OF CONTENTS

Page

TABLE OF CONTENTS i

TABLEOF AUTHORITIES ii

I. THE SEVENTH CIRCUIT ADOPTED AN UNPRECEDENTED RULE OF PER SE LEGALITY FOR EXCLUSIVE VERTICAL SUPPLY CONTRACTS 1

II. THE SEVENTH CIRCUIT'S DECISION CONFLICTS WITH THE DECISIONS OF THIS COURT AND OTHER CIRCUITS 5

III. THE SEVENTH CIRCUIT ERRED BY REFUSING TO FOLLOW THIS COURT'S DECISION IN *MOTION PICTURE ADVERTISING* 7

IV. THE SEVENTH CIRCUIT VIOLATED RULE 12(b)(6) BY RESTING ITS DECISION ON FACTUAL PRESUPPOSITIONS CONTRARY TO THE CRUCIAL ALLEGATIONS OF THE COMPLAINT 9

CONCLUSION 10

TABLE OF AUTHORITIES

Page

CASES

Chicago Professional Sports Ltd. Partnership v. Nat'l Basketball Ass'n, 95 F.3d 593 (7th Cir. 1996) 4

Eastman Kodak Co. v. Image Technical Services, Inc., 504 U.S. 451 (1992) 10

FTC v. Motion Picture Advertising Service Co., 344 U.S. 392 (1953) 7

Futurevision Cable Sys. of Wiggins v. Multivision Cable TV Corp., 789 F. Supp. 760 (S.D. Miss. 1992), *aff'd without published opinion*, 986 F.2d 1418 (5th Cir. 1993) 6

NCAA v. Bd. of Regents, 468 U.S. 85 (1984) 4

Orson, Inc. v. Miramax Film Corp., 79 F.3d 1358 (3d Cir. 1996) 6

Tampa Electric Co. v. Nashville Coal Co., 365 U.S. 320 (1961) 7

U.S. Football League v. Nat'l Football League, 842 F.2d 1335 (2d Cir. 1988) 4

Woodbury Daily Times Co. v. Los Angeles Times-Washington Post News Service, Inc., 616 F. Supp. 502 (D.N.J. 1985), *aff'd without opinion*, 791 F.2d 924 (3d Cir. 1986) 5

STATUTES

15 U.S.C. § 1 1

15 U.S.C. § 14 7

TABLE OF AUTHORITIES – Continued

Page

RULES

Rule 12(b)(6), F.R.Civ.P. 1, 5, 6, 9

MISCELLANEOUS

Areeda, Phillip E., Antitrust Law (1989), Vol. VIII ...8, 9

Easterbrook, Frank H., *The Limits of Antitrust*, 63 Tex.L.Rev. 1 (1984)..... 4

Easterbrook, Frank H., *Vertical Arrangements and the Rule of Reason*, 53 Antitrust L.J. 135 (1984)..... 4

REPLY TO BRIEF IN OPPOSITION

Petitioner Paddock Publications, Inc. ("Paddock") submits this reply to the Brief of Respondents in Opposition ("Br.Opp."). All of respondents' contentions are contradicted by one undeniable reality: Applying its economic theory, the Seventh Circuit held that the exclusive vertical licenses in question had to be undertaken to maximize profits and so could not violate Section 1 of the Sherman Act, 15 U.S.C. § 1. By affirming dismissal under Rule 12(b)(6), F.R.Civ.P., of a complaint that alleges with particularity all the elements of a Rule of Reason case under Section 1, the Seventh Circuit has created a new principle of *per se* legality for such vertical agreements. The Court of Appeals reached its result by presupposing "facts" that are contradicted by the allegations of Paddock's complaints and evidence submitted in opposition to respondents' alternative motion for summary judgment. Both the Seventh Circuit's result and the method by which it reached that result demand review and reversal by this Court.

I. THE SEVENTH CIRCUIT ADOPTED AN UNPRECEDENTED RULE OF PER SE LEGALITY FOR EXCLUSIVE VERTICAL SUPPLY CONTRACTS

Respondents contend that the District Court and the Seventh Circuit, far from creating a new principle that vertical exclusive licenses are virtually always legal, merely applied the Rule of Reason and concluded that Paddock had "failed to allege any cognizable anticompetitive effects from the exclusive licenses at issue." Br.Opp. 4-5. In fact, the District Court explicitly stated that it had *not* applied the Rule of Reason, App. 85 n. 13, and the Seventh Circuit did even mention the Rule of Reason in its opinion. Moreover, it is unquestionable that

Paddock has alleged specific anticompetitive effects of the licenses:

> The exclusive licenses obtained by the *Tribune* and the *Sun-Times* from the other defendants have adversely affected consumers, advertisers, and competition in the Chicago Area Market by:
>
> (a) creating unnatural barriers to entry into the Chicago Area Market by denying the *Daily Herald* and other potential competitors access to supplemental news services and features necessary for a full and effective entry into that market and the ability to compete with the *Tribune* and the *Sun-Times*;
>
> (b) lessening the supply of news, opinions, and features available to readers in the Chicago Area Market;
>
> (c) preventing competition among the *Daily Herald*, the *Tribune* and the *Sun-Times* that would exist but for readers' desire to obtain news reports and features in their newspaper that are not available to the *Daily Herald* due to the defendants' exclusive agreements;
>
> (d) depriving readers of the *Daily Herald* who do not wish to buy more than one general interest newspaper access to popular features which they could obtain through the *Daily Herald* but for the exclusive agreements; and
>
> (e) preventing further competition for advertisers in the Chicago Area Market that would exist if the *Daily Herald* were unhindered by the exclusive agreements. App. 110-111.

Plainly, Paddock's case was not and could not be dismissed for failure to plead injury to competition and consumer welfare. The exclusive licenses maintain the Tribune's and Sun-Times' market power, limit the amount of competition and newspapers sold, create disincentives

for innovation and creativity, and allow the dominant newspapers to maintain prices higher than competitive levels.

To the contrary, the Seventh Circuit's decision is undeniably based on *per se* legality, and that fact is demonstrated by respondents' own description of the Seventh Circuit's ruling. Respondents explain that the Seventh Circuit's decision is founded on three holdings: (1) that the licenses in question serve "procompetitive purposes"; (2) that the licenses constitute "a form of exclusive distributorship"; and (3) that the shortness of the licenses' terms offered Paddock the opportunity to compete. Br.Opp. 4. But these are all disputed factual issues. The Magistrate Judge, who unlike the District Court and Court of Appeals, actually examined Paddock's evidence in recommending denial of respondents' alternative motion for summary judgment, found the procompetitive justifications offered by respondents to be "pure speculation."[1] App. 50. He flatly rejected the idea that the exclusive licenses create exclusive distributorships. App. 35-40. Paddock also submitted abundant evidence, from respondents' own witnesses, that the system of licensing actually in practice in this country does not re-open the licenses for bidding after the initial term has expired. App. 202, 210-213, 216-220, 228-230, 243-249, 271. As one of respondents' witnesses explained:

---

[1] Respondents state that "the Seventh Circuit was able to *discern* only procompetitive effects" of the licenses on interbrand competition. Br.Opp. 8 (emphasis added). On the basis of what? Certainly nothing in the complaint, amended complaint, or summary judgment record supports such a conclusion. The Seventh Circuit was instead making a legal holding that such licenses are always procompetitive regardless of the facts.

> What we do is we enter into an agreement, an exclusive agreement, and say for instance that it's 30 days. Somebody has to actively cancel that contract in order for it to change. We would not as a normal practice if a feature becomes popular go in and cancel a contract on anybody that has bought the feature unless there was some very unusual circumstances. It has been very few times in the industry. App. 211.

If, as respondents claim, the Seventh Circuit had applied the Rule of Reason in this case, then it was a novel "no look" version; it was plainly not the "full look" or "quick look" applications of the Rule of Reason that this Court has developed.[2] Instead, the Court of Appeals followed Judge Easterbrook's lead and adopted as law his long-held views that the Rule of Reason should be scrapped and that vertical agreements are virtually always legal. Frank H. Easterbrook, *Vertical Arrangements and the Rule of Reason*, 53 Antitrust L.J. 135, 168 (1984); Frank H. Easterbrook, *The Limits of Antitrust* 63 Tex.L.Rev. 1 (1984).[3]

---

[2] *See NCAA v. Bd. of Regents*, 468 U.S. 85, 104-113 (1984); *Chicago Professional Sports Ltd. Partnership v. Nat'l Basketball Ass'n*, 95 F.3d 593, 600 (7th Cir. 1996).

[3] Respondents merely repeat the Seventh Circuit's non sequitur that because the exclusive licenses in question would not violate the "essential facility" doctrine they also cannot violate the Rule of Reason. Br.Opp. 7. The two antitrust rules have completely different elements. *See, e.g., U.S. Football League v. Nat'l Football League*, 842 F.2d 1335, 1353, 1368-1369 (2d Cir. 1988). While the essential facility doctrine deals with a monopolist's control of a "bottleneck" facility, this case involves restraints created by contracts between the dominant newspapers and the major suppliers of news service material and features. As the Magistrate Judge observed, there is no

II. THE SEVENTH CIRCUIT'S DECISION CONFLICTS WITH THE DECISIONS OF THIS COURT AND OTHER CIRCUITS

Respondents focus on two cases to attempt to show that the Seventh Circuit's refusal to apply the Rule of Reason is consistent with decisions of other Circuits. Br.Opp. 10-13. They could not have selected more inapt examples. Both were summary judgments, not Rule 12(b)(6) dismissals, and both turned upon the facts, not *per se* legality.

In *Woodbury Daily Times Co. v. Los Angeles Times-Washington Post News Service, Inc.*, 616 F. Supp. 502 (D.N.J. 1985), *aff'd without opinion*, 791 F.2d 924 (3d Cir. 1986), the plaintiff newspaper did not even claim that the exclusive news service license in question injured competition but instead the exact opposite: that the plaintiff was *not* in competition with the Philadelphia Inquirer which held that license. 616 F. Supp. at 506. Furthermore, the plaintiff complained about its inability to obtain the Los Angeles Times/Washington Post News Service because of the exclusive license held by the Inquirer even though the New York Times News Service was available. *Id.* at 511. The plaintiff made no showing of why the New York Times News Service would not be an adequate substitute. *Woodbury* turned on the factual record developed by the parties in that case and cannot be stretched to fit the very different facts of this case. Paddock alleges that it cannot obtain the New York Times News Service or the Los

---

natural bottleneck here: "[I]nformation can be replicated indefinitely; nonexclusive licensing poses no logistical problems." App. 58.

Angeles Times/Washington Post News Service *because the Daily Herald is in competition* with the Tribune and Sun-Times, and there are no adequate substitutes available to Paddock. The Magistrate Judge found *Woodbury* inapplicable here. App. 44-47.

The decision in *Orson, Inc. v. Miramax Film Corp.*, 79 F.3d 1358, 1372 (3d Cir. 1996), also turned entirely on the facts: The Third Circuit concluded that the plaintiff theater "failed to present sufficient evidence to support its claim. . . . " The Court stressed that the record showed that it was "the indisputable existence of alternative sources of supply . . . which negates the existence of anticompetitive effects in this case." *Id.* Here, Paddock does have the evidence to back up its claim that it does not have access to news services and features of sufficient quality to enable it to compete with the Tribune and Sun-Times. App. 145-146, 153, 156, 159-160, 194-196. However, under the decisions below, Paddock will never have the opportunity to offer such evidence.

The only case cited by respondents (in a footnote, Br.Opp. 10 n. 19) in which an antitrust claim was dismissed under Rule 12(b)(6) is *Futurevision Cable Sys. of Wiggins v. Multivision Cable TV Corp.*, 789 F. Supp. 760 (S.D.Miss. 1992), *aff'd without published opinion*, 986 F.2d 1418 (5th Cir. 1993), but the complaint there did not claim that the exclusive licenses in question had blocked the plaintiff cable television system operator from obtaining vital programming. The plaintiff cable system had access to all cable programs except The Learning Channel and ESPN Sunday Night Football and did not allege that it lacked adequate substitutes even for those programs. 789 F. Supp. at 769-771. The plaintiff even admitted in its complaint that it had achieved "remarkable success in securing cable subscribers. . . . " *Id.* at 769.

The other Circuits, therefore, have not adopted the Seventh Circuit's *per se* rule of vertical legality. They have instead taken the old-fashioned approach of giving complaint allegations and facts real significance under the antitrust laws.

III. THE SEVENTH CIRCUIT ERRED BY REFUSING TO FOLLOW THIS COURT'S DECISION IN *MOTION PICTURE ADVERTISING*

In addition to echoing the Seventh Circuit's invalid effort to denigrate and distinguish this Court's decision in *FTC v. Motion Picture Advertising Service Co.*, 344 U.S. 392 (1953), respondents contend that *Tampa Electric Co. v. Nashville Coal Co.*, 365 U.S. 320 (1961), marked a change in the approach to exclusive dealing that placed less stress on market foreclosure. Br.Opp. 14 n. 20. *Tampa Electric*, however, did not in the least bit undermine *Motion Picture Advertising*. This Court in *Tampa Electric* adopted an approach very similar to the Rule of Reason for evaluating exclusive dealing arrangements under Section 3 of the Clayton Act, 15 U.S.C. § 14, and specifically pointed out the significance of "an industry-wide practice of relying upon exclusive contracts. . . . " 365 U.S. at 334.

Respondents (as well as the District Court and Court of Appeals) glaringly fail to offer any reason why it should not be significant under the Rule of Reason that the two dominant newspapers in the Chicago market, each with market power, use similar exclusive dealing contracts to suppress competition, and the aggregate effect of the exclusive agreements has achieved the anti-competitive purpose of foreclosing competition from the Daily Herald. Respondents cite no authorities supporting the Seventh Circuit's refusal to consider the aggregate

anticompetitive effects of the major firms' exclusive contracts in deciding whether they violate the Rule of Reason.

Respondents rely heavily on the Seventh Circuit's extraordinary conception that the newspapers should be deemed "distributors" of the news services and features they license. Br.Opp. 15-16. Yet they ignore the fact, demonstrated conclusively in the Petition at 22-23, that the Seventh Circuit's distributorship model contradicts the allegations of Paddock's complaint, which cannot be gainsaid on a Rule 12(b)(6) motion, as well as evidence offered by Paddock and the Magistrate Judge's conclusion that the model does not fit this case. But, ironically, the law with respect to distributorships does not help them on the aggregation issue. Respondents cite Areeda to defend the legitimacy of "sole outlet" distributorships, Br.Opp. 16-17 n. 35, but omit reference to his discussion of the great anticompetitive danger created when the major firms in a market all use the same vertical restraints:

> *Cumulative market coverage.* When used by all manufacturers, distribution restraints could severely narrow interbrand competition at the dealer level and thereby increase the restraint's attractiveness to the dealers and magnify any adverse welfare consequences the restraint might have. . . . [W]idespread coverage is a "strong" indicator of a significant likelihood that the restraint serves anticompetitive dealer interests, and even those who are sympathetic to vertical distribution restraints acknowledge that this danger increases with market coverage.

VIII Phillip E. Areeda, Antitrust Law ¶ 1604f4 (1989) at 62 (footnote omitted).

Thus, even if the record were altered to superimpose a distributorship model on the newspaper industry, the aggregation (or in Areeda's term, "cumulative") principle remains valid. More appropriate in this case, however, is Areeda's condemnation of a buyer's exclusive contract "foreclosing its rivals from needed supplies in order to obtain or reinforce its own power. . . . " *Id.*, ¶ 1652c, at 572-573. The exclusive licenses here are designed to foreclose the Daily Herald from needed supplies and preserve the duopoly in the Chicago area newspaper market.[4]

IV. THE SEVENTH CIRCUIT VIOLATED RULE 12(b)(6) BY RESTING ITS DECISION ON FACTUAL PRESUPPOSITIONS CONTRARY TO THE CRUCIAL ALLEGATIONS OF THE COMPLAINT

Respondents refuse to address the significance of the Seventh Circuit's reliance on its own outside-the-record factual determinations in affirming a Rule 12(b)(6) dismissal. Paddock does not ask the Court, as respondents contend (Br.Opp. 18-19 n. 40), to decide factual issues. Instead, Paddock asks the Court to reverse the Seventh Circuit because it disdained the federal judicial process and dismissed this case on the basis of the panel's personal beliefs about competition in the newspaper industry rather than the well-pleaded facts and the record. The

---

[4] Respondents' contention (Br.Opp. 16 n. 34) that Paddock described the exclusive licenses for the first time in its Petition as exclusive supply contracts is completely wrong. Paddock has always viewed the news services and features in question as vital ingredients of a general interest newspaper. App. 95, 100, 105, 110-111, 121, 129. The Magistrate Judge reached the same conclusion after examining the evidence. App. 35-40.

Seventh Circuit simply did not believe Paddock's factual allegations of injury to competition and thus threw the case out without first requiring the District Court to examine the evidence and make the necessary findings. Rather than assume the facts alleged in Paddock's complaint to be true, the Seventh Circuit found its own facts. Although inappropriate in any case, this approach is particularly perverse in an antitrust case. This Court has never deviated from its insistence that antitrust cases be decided on their particular facts. *Eastman Kodak Co. v. Image Technical Services, Inc.*, 504 U.S. 451, 466-467 (1992). The Seventh Circuit's handling of this case cannot be countenanced under basic concepts of fairness to a litigant.

CONCLUSION

This case presents the Court with fundamental issues under the antitrust laws and the Federal Rules of Civil Procedure. Accordingly, Paddock asks the Court to grant the Petition, reverse the decision below, and remand this case for the trial to which Paddock is entitled.

Respectfully submitted,

LEE A. FREEMAN, JR.
Counsel of Record
JAMES T. MALYSIAK
FREEMAN, FREEMAN & SALZMAN, P.C.
401 North Michigan Avenue
Suite 3200
Chicago, Illinois 60611-4207
(312) 222-5100

Counsel for the Petitioner

Dated: May 23, 1997